

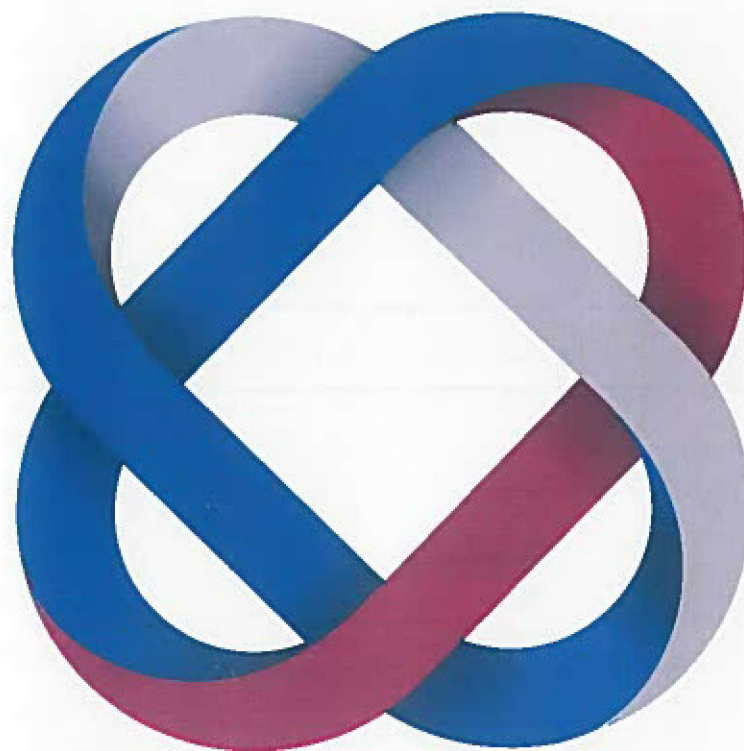
Public Disclosure Authorized

# Financial Statements and Independent Auditor's Report

Renewable Resources and Energy Efficiency Fund

Geothermal Exploratory Drilling Project SCF-SREP  
Grant No. TF0A0544

As of and for the year ended 31 December 2017



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# Independent auditor's report

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To the board of trustees of the Renewable Resources and Energy Efficiency Fund,

## *Opinion*

We have audited the accompanying project financial statements of the Geothermal exploratory drilling project (the "Project"), financed by the International Bank for Reconstruction and Development (the "IBRD") acting as an implementing agency of the Scaling-up Renewable Energy Program (the "SREP") under the Strategic Climate Fund (the "SCF") Grant Agreement SCF-SREP Grant No. TF0A0544, which comprise the statement of financial position as of 31 December 2017, the statement of the Project sources and uses of funds, the statement of uses of funds by Project activities, the designated account statement as of and for the year ended 31 December 2017 as well as the statement of expenditures ("SOE") submitted to the World Bank for the year ended 31 December 2017 in support of the Grant Agreement SCF-SREP Grant No. TF0A0544 withdrawals, and a summary of significant accounting policies and other explanatory information.

In our opinion, the project financial statements are prepared, in all material respects, in accordance with the accounting policies described in note 2 to the project financial statements, the World Bank guidelines, and the relevant points of the Grant Agreement SCF-SREP Grant No. TF0A0544.

In addition, in our opinion, the SOEs submitted together with the internal controls and procedures involved in their preparation can be relied upon to support the applications for the Grant Agreement SCF-SREP Grant No. TF0A0544 withdrawals.

## *Basis for Opinion*

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Project Financial Statements section of our report. We are independent of the "Renewable Resources and Energy Efficiency Fund" (the "R2E2 Fund") in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in the Republic of Armenia, and we have fulfilled our other ethical responsibilities in accordance with those ethical requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## *Emphasis of Matters*

- We draw attention to note 2 to the project financial statements, which describes the basis of accounting. The project financial statements are prepared to assist the management of the Renewable Resources and Energy Efficiency Fund to meet the requirements of the financial reporting of the World Bank. As a result, the project financial statements may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

- We draw attention to note 9 to the accompanying project financial statements, which describes the changes in the political situation of the Republic of Armenia. Although there is certain political instability at present, management of the R2E2 Fund does not consider that it will have a significant impact on the Project's performance, direction and continuity. The possible effects of this matter cannot be estimated as at the date of this report, therefore these project financial statements do not include adjustments resulting from it. Our opinion is not modified in respect of this matter.

***Responsibilities of Management and Those Charged with Governance for the Project Financial Statements***

Management is responsible for the preparation and fair presentation of the project financial statements in accordance with the accounting policies described in note 2 to the project financial statements, the World Bank guidelines, and the relevant points of the Grant Agreement SCF-SREP Grant No. TF0A0544, and for such internal control as management determines is necessary to enable the preparation of project financial statements that are free from material misstatement, whether due to fraud or error.

Those charged with governance are responsible for overseeing the Project's financial reporting process.

***Auditor's Responsibilities for the Audit of the Project Financial Statements***

Our objectives are to obtain reasonable assurance about whether the project financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these project financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the project financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the R2E2 Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Evaluate the overall presentation, structure and content of the project financial statements, including the disclosures, and whether the project financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the management, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Gagik Gyulbudaghyan

Managing Partner

15 June 2018

Emil Vassilyan, FCCA

Engagement Partner



# Statement of financial position

US dollars	Note	As of 31 December 2017	As of 31 December 2016
<b>Assets</b>			
<i>Current assets</i>			
Balances in bank accounts			
Designated account		594,817	243,576
		<u>594,817</u>	<u>243,576</u>
<i>Non-current assets</i>			
Accumulated Project expenses		7,838,515	7,590,553
Advance		413	-
		<u>7,838,928</u>	<u>7,590,553</u>
<b>Total assets</b>		<u><b>8,433,745</b></u>	<u><b>7,834,129</b></u>
<i>Funds and liabilities</i>			
Accumulated Project financing		8,412,516	7,653,616
Exchange rate difference		21,229	25,014
		<u>8,433,745</u>	<u>7,678,630</u>
<i>Current liabilities</i>			
Accounts payable	4	-	155,499
<b>Total funds and liabilities</b>		<u><b>8,433,745</b></u>	<u><b>7,834,129</b></u>

The project financial statements were approved on 15 June 2018 by:

Ruben Gevorgyan  
Director

Siranush Gorgyan  
Financial Manager



This statement is to be read in conjunction with the notes to and forming part of the special purpose project financial statements set out on pages 10 to 14.

# Statement of the Project sources and uses of fund

Grant Agreement TF0A0544  
As of and for the year ended 31 December 2017

In US dollars

	Actual		Planned		Variance		Life of Project
	For the year	As of 31 December 2017	For the year	As of 31 December 2017	For the year	As of 31 December 2017	
<b>Sources of funds</b>							
IBRD Grant Number TF 0A0544 (note 5)	613,896	6,853,833					
Government co-financing	145,004	1,558,683					
<b>Total</b>	<b>758,900</b>	<b>8,412,516</b>					
Exchange rate difference	(3,785)	21,229					
<b>Less: Uses of funds</b>							
Goods, works, non-consulting services, consultants' services and operating costs under the Project (note 6)	247,962	7,838,515	2,500,034	10,193,155	(2,252,072)	(2,354,640)	10,687,500
<b>Total</b>	<b>247,962</b>	<b>7,838,515</b>	<b>2,500,034</b>	<b>10,193,155</b>	<b>(2,252,072)</b>	<b>(2,354,640)</b>	<b>10,687,500</b>
<b>Net increase in working capital (note 7)</b>	<b>507,153</b>	<b>595,230</b>					

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14.

# Statement of uses of funds by Project activities

Grant Agreement TFOA0544  
As of and for the year ended 31 December 2017

In US dollars

	Actual		Planned		Variance		Life of Project
	For the year	As of 31 December 2017	For the year	As of 31 December 2017	For the year	As of 31 December 2017	
A.1.1 Construction of access road and other associated infrastructure	-	1,442,291	-	1,522,305	-	(80,014)	1,508,086
A1.2. Drilling of slim exploratory wells	-	5,443,028	-	5,454,723	-	(11,695)	4,429,825
A.2.1. Well logging and well testing	138,028	490,886	139,826	481,850	(1,798)	9,036	217,243
A.2.2 Technical supervision and support	13,556	348,613	13,556	370,269	-	(21,656)	208,334
A2.3. Project audit and operating costs	19,977	37,296	19,977	37,333	-	(37)	31,250
B.1.1. Construction of water infrastructure and rig pad	-	-	-	-	-	-	260,416
B.1.2. Drilling of production-size exploratory well	-	-	2,250,274	2,250,274	(2,250,274)	(2,250,274)	2,773,438
B.2.1. Well logging, mud logging and well testing	-	-	-	-	-	-	373,493
B.2.2. Feasibility study for a potential geothermal power plant	28,842	28,842	28,842	28,842	-	-	302,082
B.2.3. Technical supervision and support consultant	-	-	-	-	-	-	312,500
B.2.4. Transaction advisory support	-	-	-	-	-	-	208,333
B2.5. Project audit and operating costs	47,559	47,559	47,559	47,559	-	-	62,500
<b>Total</b>	<b>247,962</b>	<b>7,838,515</b>	<b>2,500,034</b>	<b>10,193,155</b>	<b>(2,252,072)</b>	<b>(2,354,640)</b>	<b>10,687,500</b>

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14.

# SOE withdrawal schedule

Grant Agreement TF0A0544  
For the year ended 31 December 2017

In US dollars

Application No.	Category
	Goods, works, non-consulting services, consultants' services and operating costs under the Project
15-DA	121,166
16-DA	59,514
17-DA	19,413
Total	200,093

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14.



# Designated account statement

Grant Agreement TFOA0544  
As of and for the year ended 31 December 2017

In US dollars

Opening balance as of 1 January 2017		243,576
Add:		
Grant replenishment during the year	613,896	<u>613,896</u>
	<u>613,896</u>	<u>613,896</u>
Present outstanding amount advanced to the designated account (1)		<u>857,472</u>
Closing balance as of 31 December 2017		594,817
Add:		
Amount of eligible expenditures paid during the year	262,655	
Service charges (if applicable)	-	
	<u>262,655</u>	<u>262,655</u>
Total advance accounted for (2)		<u>857,472</u>
Discrepancy (1) – (2) to be explained		-

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14.

# Notes to the Project financial statements

## 1 Activity

Renewable Resources and Energy Efficiency Fund (the "Fund") has been established on 21 November 2005, in accordance with the decree N799 of the Government of the Republic of Armenia ("RA") dated 28 April 2005.

The Fund implements the Geothermal exploratory drilling project (the "Project"), which is financed under the Grant Agreement SCF-SREP Grant No. TFOA0544 signed between the International Bank for Reconstruction and Development (the "IBRD") acting as an implementing agency of the Scaling-up Renewable Energy Program (the "SREP") under the Strategic Climate Fund (the "SCF") and the Government of the Republic of Armenia on 16 June 2015.

The objective of the Project is to confirm whether the geothermal resource at the Project site is suitable for power generation and, if confirmed, to involve the private sector in the development of the geothermal power plant.

The Project consists of the following phases:

### Phase 1

#### A.1. Construction of Access Road and First Phase of Exploratory Drilling

##### **A.1.1. Construction of access road and other associated infrastructure**

Carrying out the following activities to facilitate the drilling activities under Phase 1 A.1.2 of the Project: (a) construction of a gravel road with sufficient length and width to allow for safe transportation of equipment and other materials to the Project Site; (b) preparation of rig pads for slim-size wells; and (c) installation of equipment and minor works at the water source.

##### **A.1.2. Drilling of slim exploratory wells**

Drilling of up to two slim-size wells.

#### A.2. Technical Assistance and Supervision

##### **A.2.1. Well logging and well testing**

Carrying out the following activities: during the implementation, and at the completion of, activity under Phase 1 A.1.2. above, including, inter-alia: (i) analyses of the cuttings from the borehole, well temperature, and pressure measurements; and (ii) gathering of essential data such as drilling progress and changes in temperature during, and at the end of, each drilling stage.

##### **A.2.2. Technical supervision and support**

(i) Providing technical assistance for the supervision of the activity under Phase 1 A.1.2 above; (ii) providing technical support in the review of the information obtained from the completion of the activity under Phase 1 A.2.1 above; (iii) providing other technical advice and support during the implementation of this Phase 1, as required by the R2E2 Fund; and (iv) preparing the Technical Report.

##### **A.2.3. Project audit and Operating Costs**

Carrying out Project audits and financing Operating Costs for Phase 1 of the Project.

## Phase 2

### **B.1. Construction of Water Infrastructure, Rig Pads and Second Phase of Exploratory Drilling**

#### **B.1.1. Construction of Water Infrastructure and Rig Pad**

Carrying out the construction of (i) infrastructure to supply water for the drilling activities under Phase 2 B.1.2. below; and (ii) a rig pad(s) for production-size well(s).

#### **B.1.2. Drilling of production-size exploratory well**

Drilling of at least one production-size well.

### **B.2. Technical Assistance and Supervision**

#### **B.2.1. Well logging, mud logging and well testing**

Carrying out the following activities during implementation, and at the completion of, the activity under Phase 2 B.1.2. above, including, inter-alia: (i) analysis of the cuttings from the borehole, well temperature and pressure measurements; and (ii) gathering of data such as drilling progress and changes in temperature during, and at the end of, each drilling stage.

#### **B.2.2. Feasibility study for a potential geothermal power plant**

Carrying out a feasibility study of a potential geothermal power plant (excluding construction), which will include, inter-alia: (i) a technical viability assessment of a potential geothermal power plant; and (ii) an assessment of the economic and financial viability of a potential geothermal power plant.

#### **B.2.3. Technical supervision and support**

(i) Providing technical assistance for the supervision of the activity under Phase 2 B.1.2 above; (ii) providing technical support in the review of the information obtained from the completion of the activity under Phase 2 B.2.1 above; and (iii) providing other technical advice and support during the implementation of this Phase 2 as required by the R2E2 Fund.

#### **B.2.4. Transaction advisory support**

Providing advisory services to the Recipient on the design and implementation of a public-private partnership (PPP) scheme in the construction and operation of a potential geothermal power plant.

#### **B.2.5. Project audit and operating costs**

Carrying out Project audits and financing Operating Costs for Phase 2 of the Project.

In accordance with the Grant Agreement the financing of the Project is implemented through the following category:

Category	Percentage of expenses to be financed	Amount of the grant allocated (in USD)
Goods, works, non-consulting services, consultants' services and operating costs under the Project	80 %	8,550,000
Total		8,550,000

The legal address of the Fund is Melik Adamyan 1, Yerevan, Armenia.

The average number of the Fund's staff in 2017 was 21 (2016: 15).

## 2 Significant accounting policies

### 2.1 Basis of preparation

The project financial statements were prepared in accordance with the accrual basis of accounting as well as the World Bank guidelines and the relevant points of the Grant Agreement SCF-SREP Grant No. TF0A0544. Significant accounting policies are disclosed below.

### 2.2 Functional and presentation currency

The national currency of the Republic of Armenia is Armenian dram. These project financial statements are presented in US dollars (presentation currency).

In preparing the project financial statements, transactions in currencies other than US dollar are recorded at the rates of exchange defined by the Central Bank of Armenia prevailing on the dates of the transactions. For direct payments denominated in currencies other than US dollar to the contractor/consultant from the World Bank share, the exchange rate set out for the presentation of the operation in the system client connection (<https://clientconnection.worldbank.org>) is used. At each reporting date, bank balances, advances and payables denominated in foreign currencies are retranslated at the rate defined by the Central Bank of Armenia prevailing on that date, which is 484.10 Armenian drams for 1 US dollar as of 31 December 2017 (as of 31 December 2016: 483.94 Armenian drams for 1 US dollar). Any exchange rate differences are recognized in the statement of the Project sources and uses of funds and the accumulated figure of exchange rate difference is disclosed in the Statement of financial position under "Exchange rate differences".

### 2.3 Project financing

The financing received in the framework of the Grant Agreement SCF-SREP Grant No. TF0A0544 is recorded in the statement of financial position as "Accumulated Project financing" and is recognized at each replenishment. In addition, the current period funds received are disclosed in the statement of Project sources and uses of funds, showing the sources of funds.

### 2.4 Project expenses

The Project expenses are recognized on the accrual basis of accounting. The accumulated Project expenses are disclosed in the statement of financial position under non-current assets. In addition, current period expenses are disclosed in the statement of Project sources and uses of funds and statement of uses of funds by Project activity, both by category and by activities. Additionally, a further breakdown of expenses by categories is disclosed in note 6.

### 2.5 Accounts payable

Payables comprise the amounts to be paid and are stated at nominal value.

### 2.6 The World Bank financing

To finance eligible expenditures for the Grant Agreement SCF-SREP Grant No. TF0A0544, the World Bank disburses proceeds from the Credit account using one or more of the disbursement methods, which are stated below:

a. Reimbursement

The Bank may reimburse the borrower to finance eligible expenditures that the borrower has prefinanced from its own resources.

b. Advance

The Bank may advance loan proceeds into a designated account of the borrower to finance eligible expenditures as they are incurred and for which supporting documents will be provided at a later date.

c. Direct payment

The Bank may make payments, at the borrower's request, directly to a third party for eligible expenditures.

d. Special commitment

The Bank may pay amounts to a third party for eligible expenditures under special commitments entered into, in writing, at the borrower's request and on terms and conditions agreed between the Bank and the borrower.

### 3. Closing date of the Project

The closing date of the Project was defined as May 31, 2019.

### 4. Accounts payable

In US dollars	As of 31 December 2017	As of 31 December 2016
Payables to the Fund	-	80,129
Payables to suppliers	-	75,370
	-	155,499

Payable to the Fund include the amounts to be paid to the Fund, since the own resources of the Fund were used for the purposes of the Project.

### 5. Grant TF0A0544 (IBRD Fund)

In US dollars	For the year ended 31 December 2017	As of 31 December 2017
SOE procedures	200,093	285,417
Designated account advances	-	600,000
Direct payment	-	375,255
Reimbursement	-	216,454
Other procedures	413,803	5,376,707
	613,896	6,853,833

Under the method of "SOE procedures" of financing, the Fund requests advance to and documentation of designated account accompanied by the statement of expenditure (SOE).

Under the method of "Other procedures" of financing, the Fund requests advance to and documentation of designated account accompanied by the records evidencing eligible expenditures for payments against contracts valued at more than the amounts in accordance with the Disbursement Letter and contracts that are subject to the World Bank's prior review.

### 6. Uses of funds by category descriptions

The statement of the Project sources and uses of funds discloses the expenses in one combined category, as depicted in the Grant Agreement SCF-SREP Grant No. TF0A0544. However, for the convenience of certain users, the breakdown of the uses of funds is disclosed in the table below.

In US dollars	For the year ended 31 December 2017	As of 31 December 2017
Works	-	6,885,319
Consultants' services	180,425	885,659
Operating expenses	67,537	67,537
	247,962	7,838,515

## 7. Net increase in working capital

In US dollars

	For the year ended 31 December 2017	As of 31 December 2017
Increase in bank balances	351,241	594,817
Decrease in accounts payable	155,499	-
Increase in advances	413	413
	<u>507,153</u>	<u>595,230</u>

## 8. Reconciliation between the amounts received by the Fund and disbursed by the World Bank

Grant Agreement TFOA0544  
For the year ended December 31, 2017

In US dollars

Category	Appl.	Fund	The World Bank	Difference
Goods, works, non-consulting services, consultants' services and operating costs under the Project	15-DA	423,053	423,053	-
	16-DA	171,430	171,430	-
	17-DA	19,413	19,413	-
		<u>613,896</u>	<u>613,896</u>	-
Total		<u>613,896</u>	<u>613,896</u>	-

## 9. Subsequent event

In April-May 2018 after the resignation of the prime minister nominated and elected by the ruling political party in the National Assembly as a result of the political upheaval and disobedience of the population in the Republic of Armenia, the National Assembly nominated the popular candidate for the post of the prime minister, and accordingly, a new government was formed, which considers itself temporary until the formation of the new National Assembly through extraordinary elections. Although there is certain political instability at present, management of the R2E2 Fund does not consider that these processes will have a significant impact on the Project's performance, direction and continuity, and according to management of the R2E2 Fund, there is no necessity to adjust the financial statements of the Project as of and for the year ended 31 December 2017.